No. 76-1499

In the Supreme Court of the United States

OCTOBER TERM, 1976

CHARLES G. RODMAN, AS TRUSTEE OF THE ESTATE OF W. T. GRANT COMPANY, BANKRUPT, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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INDEX

CITATIONS

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OPINIONS BELOW

The memorandum and order of the Tax Court (Pet. App. C 46a-47a) are not reported. The opinion of the court of appeals (Pet. App. D 51a-57a) is reported at 548 F. 2d 1109.

JURISDICTION

The judgment of the court of appeals (Pet. App. D 58a) was entered on February 3, 1977. The petition for a writ of certiorari was filed on April 28, 1977. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the court of appeals correctly adhered to its prior decision that W. T. Grant Company's sales of books containing coupons that could be exchanged for

merchandise did not qualify for installment sales tax treatment under Section 453 of the Internal Revenue Code of 1954 and the Treasury Regulations promulgated thereunder.

STATUTE AND REGULATIONS INVOLVED

The pertinent portions of Section 453 of the Internal Revenue Code of 1954 (26 U.S.C.) and of Treasury Regulations on Income Tax, Sections 1.453-1 and 1.453-2 (26 C.F.R.), are set forth at Pet. App. E 59a and Pet. App. F 60a-85a.

STATEMENT

Prior to its adjudication in bankruptcy, W. T. Grant Company sold a wide variety of merchandise at retail in stores located throughout the United States (Pet. App. A 3a). The company sold merchandise on three types of credit plans: (1) a traditional installment plan, referred to as the Special Purchase Installment Plan; (2) a revolving credit plan, referred to as the 30-day Option Plan; and (3) the Coupon Book Installment Plan (Pet. App. B 38a).

Under the Coupon Book Installment Plan, customers purchased coupon books containing coupons redeemable at face value for merchandise in any Grant's store. Grant issued coupon books with aggregate values of coupons ranging from $10 to $100. The customer could pay for a book of coupons in full at the time of purchase, or he could execute a retail credit agreement agreeing to pay the aggregate face value of the book, plus a charge for delayed payment, in prescribed monthly installments, with terms varying from four to 18 months (Pet. App. B 39a-40a).

If the customer returned coupons or merchandise, the amount due for the coupon book and the delayed payment charge would be reduced. The customer could pay a monthly installment in advance, but such a prepayment did

not reduce the size of subsequent installment payments. However, if the customer paid the full balance of remaining installments in advance, Grant reduced the delayed payment charge (Pet. App. A 5a-6a; Pet. App. B 40a).

On its books, Grant treated redemptions of coupons for merchandise, rather than the purchase of coupon books, as sales. Coupon books were numbered, and could be matched with particular retail credit agreements. Grant, however, did not identify and record the exchange of coupons for merchandise by each customer to whom a coupon book was issued. Therefore, it could not correlate sales of merchandise under the coupon plan with installment payments it received for books issued (Pet. App. B 40a).

On its income tax returns for its taxable years ended January 31, 1964 and 1965, Grant reported its gain from sales of merchandise under the coupon plan on the installment method prescribed by Section 453 of the Internal Revenue Code of 1954. Grant reported as income the fraction of its gross profit from the year's sales under the coupon plan that was equal to the fraction of the total price of such sales it had received in that year in the form of installment payments for coupon books (Pet. App. A 7a-9a).

Section 453 of the Code permits ratable reporting of gain from an installment sale which meets certain statutory and regulatory conditions. Under the installment method, the portion of each payment which represents taxable gain is computed by multiplying the amount of the payment by the percentage of profit on the sale.

One of the requirements for qualification under the installment method is that the sale be paid for in two or more payments. This requirement is explicitly set forth in Treasury Regulations, Section 1.453-2(b)(2) (Pet.

App. F 65a), which further states that the installment method is available for certain amounts received under revolving credit plans. With respect to such plans, Treasury Regulations, Section 1.453-2(d) (Pet. App. F 68a-72a), establishes certain minimum record-keeping requirements that must be met to qualify revolving charge plans for installment reporting, including a detailed sampling method for determining what percentage of amounts paid under revolving charge plans would qualify for installment reporting.

The Commissioner determined that under the pertinent Treasury Regulations, sales made in exchange for coupons from the books did not qualify for installment treatment as installment sales because there was no record that the sales generated by exchange of the coupons were in fact paid for in two or more installments (Pet. App. A 9a). The Tax Court upheld petitioner's claim to installment sale treatment, relying upon the "general concept" of installment sales (Pet. App. A 15a-24a).

The court of appeals, however, reversed on the authority of the Regulations (483 F. 2d 1115; Pet. App. B 36a-45a). It upheld the Commissioner's determination that under Treasury Regulations, Section 1.453-2(b)(2), Grant could not qualify for installment sale treatment unless it could submit proof that sales under its coupon book plans were actually paid for in installments, in accordance with the procedures set forth in Section 1.453-2(d) of the Regulations. Since Grant did not maintain customer redemption records for the coupon plan, the court of appeals held that it was not entitled to installment method treatment, and remanded the case to the Tax Court for computation of the deficiencies (Pet. App. B 41a-56a). This Court thereafter denied Grant's petition for a writ of certiorari (416 U.S. 937).

Prior to the commencement of the remand proceedings in the Tax Court for computation of the deficiencies, Grant moved for further trial. Although Grant conceded that it could not satisfy the standard of proof of Section 1.453-2(d) of the Regulations, it claimed it could produce evidence "consistent" with those Regulations that would qualify the vast majority of its sales under the coupon plan for installment method reporting. The Tax Court denied Grant's motion on the ground that the court of appeals required that Grant satisfy the requirements of Section 1.453-2(d) of the Regulations, and that further trial would therefore be fruitless (Pet. App. C 46a-47a). On this second appeal, the court of appeals adhered to its prior decision that Grant could report coupon plan sales on the installment method only by complying with the requirements of the Regulations, and that Grant had failed to maintain records of sales with which it could have done so (Pet. App. D 51a-57a).

ARGUMENT

1. The court of appeals correctly held that there were no special circumstances in this case that would require a departure from the rule of law it established on Grant's first appeal. As the court observed, neither the intervening bankruptcy of Grant nor the alleged resulting hardship to creditors warranted reconsideration of the legal issues already decided on the first appeal. Indeed, since 1973, three years before the bankruptcy, Grant and its creditors have been on notice that the coupon book credit plan would not receive installment tax treatment in the absence of adequate records (see Pet. App. D 54a-55a). The court of appeals therefore properly adhered to its prior decision as the law of the case. See, *e.g.*, *United States* v. *Fernandez*, 506 F. 2d 1200, 1204 (C.A. 2); *Zdanok* v. *Glidden Company, Durkee*

Famous Foods Division, 327 F. 2d 944, 952-953 (C.A. 2), certiorari denied, 377 U.S. 934.[1]

2. With respect to the merits, the court of appeals correctly held on the first appeal that Grant's coupon book credit plan does not qualify for installment sale treatment. The reasons underlying the Court's denial of Grant's prior petition for a writ of certiorari (416 U.S. 937) are equally applicable to this second petition.

Section 453 of the Internal Revenue Code provides an installment method for ratably reporting gains from the sale of property over the years in which payments are received. The installment method is a relief provision, the basic purpose of which is to defer payment of tax on gains until the proceeds of sale with which to pay the tax have been received. However, since these relief provisions are exceptions to the general rule that an accrual basis taxpayer must include in income the value of all receivables, they

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[1]Petitioner therefore errs in asserting (Pet. 20-22) that the court of appeals "arbitrarily" refused to permit him to submit evidence concerning the tax treatment accorded to other retailers allegedly using similar coupon book credit plans. The policy of finality underlying the doctrine of the law of the case precludes the introduction of a new legal issue requiring the submission of additional evidence when the unsuccessful party offers no reason why the matter could not have been raised when the case was first before the trial court. See *Crown Coat Front Co.* v. *United States*, 395 F. 2d 160 (C.A. 2), certiorari denied, 393 U.S. 853.

United States v. *Fernandez*, *supra*, upon which petitioner relies (Pet. 20), is distinguishable. There, the court of appeals revised the law of the case established on an earlier appeal because new evidence demonstrated that its earlier ruling was erroneous. Here, by contrast, petitioner sought to introduce evidence both for the purpose of raising a new legal issue and to make an additional argument concerning the construction of the pertinent Regulations—an issue the court of appeals properly concluded it had "already decided on sufficient grounds" (Pet. App. D 55a).

must be strictly construed. See, *e.g.*, *Baltimore Baseball Club, Inc.* v. *United States*, 481 F. 2d 1283 (Ct. Cl.); *Cappel House Furnishing Co.* v. *United States*, 244 F. 2d 525 (C.A. 6); *Prendergast* v. *Commissioner*, 22 B.T.A. 1259, 1262.

Under Treasury Regulations promulgated in 1963 pursuant to Section 453(a), a taxpayer is permitted to defer and report on the installment basis income derived from certain sales "on the installment plan" which qualify under one of two definitions. The first definition (Treasury Regulations, Section 1.453-2(b)(1)) permits installment reporting of sales under any plan which "by its terms and conditions, contemplates that each sale" thereunder will be paid for in two or more payments. The second definition (Treasury Regulations, Section 1.453-2(b)(2)) allows installment treatment for certain of the sales under a revolving credit plan or similar credit arrangement, which contemplates that sales of merchandise will be paid for in two or more payments, and "[w]hich sale[s] * * * in fact [are] paid for in two or more payments."

The Regulations set forth record-keeping standards which must be met in order to demonstrate what percentage of sales under the second definition "in fact" are paid for in two or more payments. Thus, with respect to revolving credit plans and similar extensions of credit, a taxpayer is required to furnish proof, in accordance with a prescribed sampling technique, of the percentage of his sales which, in fact, are paid for in two or more payments (and thus qualify under the statute) as opposed to those sales in which the customer merely charges purchases but does not utilize the revolving credit feature of the plan or incur a finance charge.

In 1964, Congress amended Section 453 of the Code by adding subsection (e), providing that the term "installment

plan" includes revolving credit plans.[2] Later that same year, however, Congess repealed that provision retroactively,[3] on the ground that the installment sale concept was such "that it would have been better to have left the Treasury Department with the opportunity to determine by regulation the extent to which sales under revolving credit type plans are to be treated as sales under installment plans." S. Rep. No. 1242, 88th Cong., 2d Sess. 5 (1964). The Committee further noted (*ibid.*) that it intended that "the term 'sales on the installment plan' be interpreted by the regulations as covering 'sales on a revolving credit type plan' to the full extent provided in the regulations issued by the Treasury Department on October 15, 1963 * * * ."[4]

In light of this history, these Regulations are unquestionably valid since they have been subjected to the scrutiny of the Congress and have received its express approval. See Section 7805(a) of the Code; *United States* v. *Correll*, 389 U.S. 299, 307; *Commissioner* v. *Stidger*, 386 U.S. 287, 296; *Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501. Thus, the court of appeals correctly determined on the first appeal that "[a]ny determination, therefore, of Grant's qualifying for §453 treatment must be made in the context of the regulations" (Pet. App. B 41a).

The court of appeals' further conclusion that petitioner's coupon books did not qualify for installment sale treatment

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[2]See Section 222(a) of the Revenue Act of 1964, 78 Stat. 75.

[3]See Section 3(b) of the Act of August 31, 1964, 78 Stat. 746.

[4]Prior to the promulgation of the Regulations, the district court in *Consolidated Dry Goods Co.* v. *United States*, 180 F. Supp. 878, 882 (D. Mass.), held that a revolving credit plan came within the "ordinary meaning and the accepted trade meaning of the words 'installment plan.' " As a result, sales made under such a plan, even if only a single payment was made for an item, qualified for installment reporting. The Regulations were issued in response to this decision.

is similarly correct. Pursuant to the coupon installment plan, a customer may obtain a coupon book worth, for example, $100, for which he agrees to make payments of $10 per month for 11 months. If he uses the entire coupon book immediately to make a large purchase, he has made a purchase that has been paid for in two or more installments. If he uses the coupons to make small purchases of $10 or less per month, however, no sale of merchandise will have been paid for in two or more payments. A plan permitting the latter pattern of purchases does not qualify under the Regulation's first definition of "installment plan," which requires that each sale be paid for in two or more installments.

Finally, the court of appeals correctly held that Grant's plan did not qualify under the second definition of the Regulations. That definition provides that sales made under an installment plan which in fact are paid for in two or more installments can qualify for installment reporting if such sales (or some proportion thereof) were in fact paid for in two or more payments. Grant, however, failed to comply with the record-keeping requirements of the Regulations, which are essential in order to establish the requisite factual basis for qualification under the second definition.

3. Petitioner contends (Pet. 9-10, 14) that Section 1.453-2(b)(2) of the Regulations covers nontraditional installment plans that are not "revolving credit plans" as that term is described in Section 1.453-2(d)(1), and that only revolving credit plans are subject to the requirements of proof prescribed by Section 1.453-2(d) of the Regulations. But any differences among the variety of nontraditional plans encompassed by Sections 1.453-2(b)(2) and 1.453-2(d)(1) of the Regulations is immaterial, as is the question whether Grant's coupon plan is a revolving credit plan. The fact remains that the rules prescribing the requirements of

proof set forth in Section 1.453-2(d) of the Regulations are the sole means by which a merchant using a high-volume nontraditional plan can qualify a portion of his sales for installment reporting, and that Grant could have employed those rules for coupon plan sales had it maintained records of its coupon redemptions.[5]

Contrary to petitioner's further contention (Pet. 17), the court of appeals did not apply Section 1.453-2(d) of the Regulations in a manner that contravenes Section 453(a)(2) of the Code. That statute provides that, except for sales under a "revolving credit type plan," the selling price of sales of personal property reportable on the installment method includes finance charges the dealer treats as part of the cash selling price for accounting purposes.

But as the legislative history makes clear, Section 453 (a)(2) was intended to permit installment reporting only for finance charges earned with respect to sales under traditional installment plans and not, as petitioner suggests (Pet. 11-12, 13), for finance charges earned with respect to sales under a nontraditional installment plan that is not a revolving credit plan as described in Section 1.453-2(d)(1) of the Regulations. See S. Rep. No. 1242, *supra*, at 3-4; 110 Cong. Rec. 20034 (1964) (remarks of Senator Hartke); 110 Cong. Rec. 20302 (1964) (remarks of Representative Mills). In using the phrase "revolving credit type plan" in Section 453(a)(2) to describe sales as to which finance charges would not be eligible for deferral, Congress was referring to

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[5]Petitioner suggests (Pet. 16) that there may be nontraditional installment plans in which the rules of the Regulations cannot be used to determine a percentage of reportable sales. But petitioner's hypothetical speculations do not detract from the undisputed fact that Grant could have determined a percentage of reportable coupon plan sales using the rules of Section 1.453-2(d) of the Regulations.

all plans "described in regulations sec. 1.453-2(b)(2)" (S. Rep. No. 1242, *supra*, at 4)—*i.e.*, to all nontraditional plans.

CONCLUSION

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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JUNE 1977.